

Covid-19 : FAQs regarding Government support for businesses facing insolvency, and associated directors' duties

The UK Government has announced that it is introducing measures to help companies and directors having to make decisions about insolvency.

What are the proposed measures and what will they mean for me?

There are two main things the government has said it will do:

- 1 The first is to change the law so that company directors will not be personally liable for the debts of the company if the directors continue to trade while they know the company is insolvent.

It is important to note that the directors' duties to the company and shareholders would remain, and the directors would still have to act in their best interests at all times.

According to the department for Business, Energy and Industrial Strategy, the proposed change to the personal liability rule is intended to "reassure directors that the difficult decisions they have to make about the future viability of their business will not have to be unduly influenced by the exceptional circumstances which are entirely beyond their control."

In practice this means that as a company director you should note that this planned relaxation of their duties will only apply to 'wrongful trading'. The government has specifically stated that "all of the other checks and balances that help to ensure directors fulfil their duties properly will remain in force", including those relating to 'fraudulent trading', 'misfeasance' and the threat of director disqualification.

It is therefore not a blanket amnesty and all other duties will continue to apply as before

- 2 The second proposed change is to introduce a 90-day moratorium on companies being liquidated.

This would mean that companies would have an additional 90 days between the company knowing it is insolvent and being wound up. The period is intended to afford otherwise viable companies extra time to find a way out of insolvency. There will be qualifying criteria and protections for creditors, though the details are not yet clear (as at 20/4/20).

If you have a concern that your company may be facing insolvency, you should seek early professional advice, from your accountant, solicitor, or a qualified Insolvency Practitioner.

What are wrongful trading provisions?

When an insolvent company continues to trade and at some time before the commencement of the winding up of that company, the director or directors knew or ought to have reached the conclusion

that there was no reasonable prospect that the company would avoid going into liquidation. If so a director could be held personally liable to make a contribution toward the debts of the company.

When will these changes take effect?

Parliament is in recess until 21 April but it is expected that legislation will be fast-tracked then and will be retrospective from the 1st March 2020 and is expected to apply for an initial period of three months.

What is likely to be the effect of the changes?

There are different schools of thought.

- A. If the coronavirus crisis - and the economic effect of it - is temporary then many otherwise healthy companies will suffer a short-term financial shock from which they may recover fully, and thrive again as the economy bounces back. It would be undesirable for such companies to be forced into liquidation and therefore assistance is proposed to help them through the crisis. This would be to the ultimate benefit of creditors, who would be more likely to be paid in full than if the companies were liquidated.
- B. On the other hand, if the crisis has longer lasting negative effects, the changes may simply make it more difficult for creditors to be paid. Companies may go deeper into insolvency before being wound up and the removal of personal liability from directors takes away one of the incentives for directors to act properly. That may tend to encourage irresponsible decision-making, with negative consequences for creditors.

In practice, the result is likely to be a mixture of both, and other, outcomes. Whether the changes are generally positive is something only time will tell.

I've heard the courts are only dealing with urgent cases. How will this affect insolvency cases?

The courts will not generally consider winding up petitions to be urgent. This means that most ordinary insolvency matters will not proceed until after the present restrictions are lifted.

However, if there is any genuine urgency – for example, where there is a significant danger of assets being lost or damaged unless they are dealt with quickly – then the courts may be persuaded to deal with the case, but perhaps only as far as is necessary to address the urgent issues.

Generally, this is likely to coincide with the test for the appointment of provisional liquidators, i.e. where a liquidator is said to be required as an emergency. The same requirement for urgency is likely to apply also to any matters incidental to an insolvency petition.

Our company is currently undergoing restructuring. How can we keep trading at this time?

The Government's new measures to help improve insolvency systems will also support those already undergoing restructuring, with the aim to help them keep trading.

Provisions include:

- to allow those who are undergoing restructuring to continue to access supplies and raw materials,
- the collection of debts from creditors will also be suspended whilst restructuring or rescue is being sought to allow for additional “breathing space” and
- a new restructuring plan, binding creditors to that plan.

We are creditors or a supplier looking to recover debts from a company proposing insolvency or a company undergoing restructuring. How would we recover debts if there is a suspension of debt payments?

The Government has proposed provisions to safeguard creditors or suppliers to ensure they are paid whilst restructuring or a solution is being obtained.

What should directors be doing now to protect their own positions and to ensure so far as possible viable continuity of their businesses?

- Records of decisions are important, so hold regular board meetings, and prepare contemporaneous minutes to document any key decision made about the ongoing operations of the business. If in doubt, directors should continue to seek advice on how to record their decision making throughout this period.
- Consider the availability of viable financial rescue measures, including those announced by the UK and Scottish governments. <https://www.gov.uk/government/publications/guidance-to-employers-and-businesses-about-covid-19/covid-19-support-for-businesses>
Those measures that government has announced are not mutually exclusive. Some are available immediately without application, while others will require an application or specified steps to be taken.

While acquiring additional debt as part of these measures may not be appropriate, other options such as seeking a capital repayment holiday, or investigating if there are any other informal arrangements that can be reached, whether with trade creditors or others, may work for the business.

Of course in the case of Government-backed loans, consideration should be given to repayment, particularly once the interest-free period on any such loan lapses.

- Review existing key contracts for, among other things, force majeure clauses
- Open and maintain dialogue with suppliers and customers over their contingency planning, which will assist in anticipating potential future issues. You may require the cooperation of those parties over this difficult period, so engage with them now.
- Undertake financial projections based on assorted possible scenarios, including worst case impacts on trade

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- Review the terms of any banking documents to establish whether financial covenants may be breached, or if other default provisions have or will be engaged, consider whether to open dialogue with creditors.
- Review leases, whether as landlord or tenant
- Where appropriate, seek specialist advice on contingency options which will better inform Directors and decision makers whether wrongful trading is a concern, and may lessen the prospect of any subsequent charge of wrongful trading.

Further advice on the impact of the Coronavirus pandemic on companies and company directors can be obtained by contacting a member of our team, who are available to assist and advise you in relation to any of the matters raised in this article.

If you require advice, whether as a director or in respect of a company, please contact :

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